Wiley Rein LLP

1776 K STREET NW
WASHINGTON, DC 20006
PHONE 202.719.7000
FAX 202.719.7049

7925 JONES BRANCH DRIVE
McLEAN, VA 22102
PHONE 703.905.2800
FAX 703.905.2820

www.wileyrein.com

July 17, 2013

Tom J. Navin
(202) 719-7487
tnavin@wileyrein.com

VIA ECFS AND ELECTRONIC MAIL

Chairwoman Mignon Clyburn
Commissioner Ajit Pai
Commissioner Jessica Rosenworcel
Federal Communications Commission
445 12th Street, SW
Washington, DC 20554

Re: White Paper of Puerto Rico Telephone Company, Inc. Concerning Legal and Policy Issues With Applying the CACM to Insular Areas filed in *Request for Connect America Fund Cost Models*, FCC Public Notice in WC Dockets 10-90 and 05-337, DA 11-2026 (Wireline Competition Bur., rel. Dec. 15, 2011)

Dear Chairwoman and Commissioners:

In the United States, approximately 18 million people lack access to broadband. Over 1.9 million of them live in Puerto Rico. The Commission has recognized that "[t]he percentage of unserved Americans living in U.S. Territories is approximately *nine times* the national average."[1] That is why in its *2011 USF Transformation Order*, the Commission recognized the unique challenges of serving non-contiguous U.S. and insular areas and specifically directed the Bureau to (1) adopt a cost model that adequately accounts for the unique costs of serving non-contiguous U.S. and insular areas; or (2) maintain existing frozen support levels for those non-contiguous U.S. and insular areas left out of the cost model. Common sense and the core statutory purpose of universal service as recognized by Congress and the full Commission therefore dictate that the Wireline Competition Bureau ("Bureau") allocate a meaningful portion of the $1.8B in Connect America Fund Phase II support to Puerto Ricans. Recent Bureau actions, however, seem to indicate that the Bureau may slash PRT's existing support for its wireline network by close to 90%, from $36.8M to $3.8M. At the same time, the Bureau plans to increase support nationwide by 67 percent, from $1.076B to $1.8B for other price cap carriers. PRT files the instant letter and attached White Paper to respectfully remind the Bureau of the Commission's directive to accommodate the "unique

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[1] *Eighth Section 706 Report*, GN Docket No.11-121, FCC 12-90, ¶ 56 (rel. Aug. 21, 2012) (emphasis added) (including American Samoa, Commonwealth of the Northern Mariana Islands, Guam, Puerto Rico, and the United States Virgin Islands as U.S. Territories).

circumstances" of insular areas,[2] which include significantly higher costs as well as significantly lower "take rates" that preclude insular providers from recovering the costs of broadband over a high percentage of households. Unfortunately, the approach that the Bureau appears to be contemplating will relegate Puerto Ricans to second-class digital citizenship and prevent the Commission from achieving its goal of universal broadband access.

Not only would such an approach by the Bureau be flawed as a matter of broadband policy for insular areas, but it also would suffer from several legal flaws which are detailed in the attached White Paper. First, the Bureau would exceed its delegated authority by ignoring the Commission's explicit instruction to make the "model and all underlying data, formulae, computations, and software associated with the model … available to all interested parties for review and comment."[3] Second, the Bureau's delegation of decision-making authority to CostQuest to build and operate the CAF II cost model would violate the D.C. Circuit's "subdelegation doctrine" and would render the entire cost model legally infirm because "black box" algorithms substantially determine the model's results. Third, the Bureau would violate the Administrative Procedure Act's ("APA") notice and comment requirements if it calculates insular support via CostQuest's proprietary CACM because it is riddled with hidden algorithms and erroneous assumptions that prevent PRT and other third parties from even attempting to evaluate the model's approach.

For the forgoing reasons, the Bureau should heed the Commission's direction and ensure that insular areas are supported by the CAF II mechanism.

Respectfully submitted,

Tom J. Navin

cc: Marlene H. Dortch, Secretary

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2 *Connect America Fund*, Report and Order, WC Docket No. 10-90, FCC 11-161, ¶ 193 (rel. Nov. 18, 2011), pets. for review pending sub nom. In re: FCC 11-161, No. 11-9900 (10th Cir. filed Dec. 18, 2011). The Commission instructed the Bureau to either: (1) adopt a cost model that adequately accounts for the unique costs of serving non-contiguous U.S. and insular areas; or (2) maintain existing frozen support levels for those non-contiguous U.S. and insular areas left out of the cost model.

3 *Id.*, ¶ 185.

Julie Veach, WCB Chief
Carol Mattey, WCB Deputy Chief
Amy Bender, WCB-TAPD Deputy Chief

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Request for Connect America Fund Cost Model	)	WC Docket No. 10-90
	)	WC Docket No. 05-337
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WHITE PAPER OF PUERTO RICO TELEPHONE COMPANY, INC. ON LEGAL AND POLICY ISSUES WITH APPLYING THE CACM TO INSULAR AREAS

Francisco J. Silva
Walter Arroyo
PUERTO RICO TELEPHONE COMPANY, INC.

By: *Thomas J. Navin*

Nancy J. Victory
Thomas J. Navin
WILEY REIN LLP
1776 K Street, NW
Washington, DC 20006
(202) 719-7000

Counsel for Puerto Rico Telephone Company, Inc.

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TABLE OF CONTENTS

I. INTRODUCTION AND EXECUTIVE SUMMARY 1

II. PURSUANT TO THE COMMISSION'S INSTRUCTIONS IN THE *2011 USF TRANSFORMATION ORDER*, THE BUREAU SHOULD EITHER USE PRT'S COST MODEL TO CALCULATE SUPPORT FOR PUERTO RICO OR FREEZE PUERTO RICO'S EXISTING SUPPORT 5

A. The CACM Fails the Commission's "Insular Test." 7

B. The BCMPR Passes the "Insular Test." 14

C. The June 10 Letter Erroneously Asserts that the Insular Carrier "Submissions Received to Date Are Insufficient." 15

D. If the Bureau Cannot Accommodate Insular Areas in its Model, it Must Maintain Frozen Support. 16

III. ANY ACTION RELYING ON THE CACM AND ITS UNDERLYING DATA WOULD EXCEED THE BUREAU'S DELEGATED AUTHORITY IF THE PUBLIC DOES NOT HAVE OPEN ACCESS TO THE CACM AND ITS UNDERLYING DATA. 17

IV. ANY USE OF THE CACM FOR INSULAR AREAS WOULD BE AN UNLAWFUL SUBDELEGATION OF DECISION-MAKING POWER TO COSTQUEST. 18

V. THE BUREAU'S RELIANCE ON A PROPRIETARY MODEL THAT IS NOT OPEN FOR PUBLIC REVIEW TO DISTRIBUTE SUPPORT TO INSULAR AREAS VIOLATES THE APA. 22

VI. CONCLUSION 24

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the Matter of	)	
	)	
Request for Connect America Fund Cost Model	)	WC Docket No. 10-90
	)	WC Docket No. 05-337
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WHITE PAPER OF PUERTO RICO TELEPHONE COMPANY, INC. ON LEGAL AND POLICY ISSUES WITH APPLYING THE CACM TO INSULAR AREAS

I. INTRODUCTION AND EXECUTIVE SUMMARY

In its *2011 USF Transformation Order*, the Federal Communications Commission ("Commission") recognized the unique challenges of serving non-contiguous U.S. and insular areas and specifically directed the Wireline Competition Bureau ("Bureau") to (1) adopt a cost model that adequately accounts for the unique costs of serving non-contiguous U.S. and insular areas; or (2) maintain existing frozen support levels for those non-contiguous U.S. and insular areas left out of the cost model.[1] The Commission's emphasis on ensuring that insular areas receive sufficient Connect America Fund ("CAF") Phase II funding is unsurprising given that in 2012 the Commission concluded that "[a]pproximately 54% of Americans residing in U.S. Territories are without access to fixed broadband meeting the speed benchmark compared to only 6 percent of Americans overall" and that "[t]he percentage of unserved Americans living in

[1] *Connect America Fund*, Report and Order, WC Docket No. 10-90, FCC 11-161, ¶ 193 (rel. Nov. 18, 2011) ("*2011 USF Transformation Order*"), Pets. for Review pending sub nom. In re: FCC 11-161, No. 11-9900 (10th Cir. filed Dec. 18, 2011).

U.S. Territories is approximately nine times the national average."[2] Yet, based on its recent actions, the Bureau may be poised to ignore the Commission's clear directive to consider the "unique circumstances" in these areas for purposes of the CAF. PRT urges the Bureau to act consistently with the Commission's delegation of authority to address the specific circumstances of insular areas.

PRT and other non-contiguous U.S. and insular carriers have endeavored, at considerable cost and effort, to inform the Bureau on how to fulfill its legal obligation to craft a CAF II distribution mechanism that adequately accounts for the unique challenges of serving non-contiguous U.S. and insular areas. Specifically, PRT and other non-contiguous U.S. and insular providers have: filed three separate cost models that accommodate non-contiguous U.S. and insular areas;[3] submitted comments in multiple CAF II rulemakings;[4] met and spoken with

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2 *Eighth Section 706 Report*, GN Docket No.11-121, FCC 12-90, ¶ 56 (rel. Aug. 21, 2012) (emphasis added) (including American Samoa, Commonwealth of the Northern Mariana Islands, Guam, Puerto Rico, and the United States Virgin Islands as U.S. Territories).

3 PRT, ACS, and VITELCO have each filed cost models.

4 *See, e.g.*, Comments of Alaska Communications Systems, WC Docket No. 10-90 (June 18, 2012); Reply Comments of VITELCO, WC Docket No. 10-90 (March 25, 2013); Comments of Sandwich Isle, WC Docket No. 10-90 (March 12, 2013); Comments of Puerto Rico Telephone Company, WC Docket No. 10-90 (March 11, 2013); Comments of Hawaiian Telcom, WC Docket No. 10-90 (March 11, 2013); Comments of General Communication, Inc., WC Docket No. 10-90 (March 11, 2013); Comments of Alaska Communications Systems, WC Docket No. 10-90 (March 11, 2013); Comments of VITELCO, WC Docket No. 10-90 (March 11, 2013); Comments of Alaska Communications Systems, WC Docket No. 10-90 (Feb. 27, 2013); Comments of VITELCO, WC Docket No. 10-90 (July 9, 2012); Reply Comments of Puerto Rico Telephone Company, WC Docket No. 10-90 (March 25, 2013); Reply Comments of Hawaiian Telcom, WC Docket No. 10-90 (March 25, 2013); Reply Comments of Alaska Communications Systems, WC Docket No. 10-90 (March 25, 2013).

Bureau staff; and regularly posted information in the CAF II Virtual Workshop.[5] Despite these efforts, PRT is concerned that the Bureau's recent actions reflect a direction in conflict with the Commission's directive to create a distinct CAF II distribution mechanism to address the unique needs of non-contiguous U.S. and insular areas. For example, on June 6, 2013, the Bureau conducted a telephone conference to encourage non-contiguous U.S. and insular carriers to supplement the record with additional cost data that show the higher costs of providing broadband service in non-contiguous U.S. and insular areas *regardless* of whether the Connect America Cost Model ("CACM") is overhauled to accurately apply to such non-contiguous U.S. and insular areas.[6] Subsequently, the Bureau appears to have eliminated the option of frozen support for these areas—one of two possible approaches endorsed by the full Commission as an outcome for the CAF Phase II proceeding—in the recent v3.1.4 Illustrative Results. Although the Bureau may still seek to accommodate insular areas in its ultimate approach, PRT is concerned that the Bureau may be signaling that it is no longer considering frozen support for non-contiguous U.S. and insular areas during CAF Phase II.[7]

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5 *See* "WCB Cost Model Virtual Workshop 2012," http://www.fcc.gov/blog/wcb-cost-model-virtual-workshop-2012 (providing links to the different questions on which PRT and other non-contiguous U.S. carriers commented).

6 The Bureau's suggestion that non-contiguous U.S. and insular carriers are not pulling their weight is baseless. *See* Letter from Dania Ayoubi, Attorney Advisor, Wireline Competition Bureau, to Marlene Dortch, WC Docket No. 10-90, at 1-2 (filed June 10, 2013) ("Wireline Bureau June 10 Letter").

7 Specifically, the Notes to the CAFII - CAM 3.1.4 - Report Version 3.0 state that the "frozen non-contiguous US support [was] not calculated with this update." "Connect America Cost Model v3.1.4 Illustrative Results," *available at http://www.fcc.gov/encyclopedia/connect-america-cost-model-illustrative-results*. This deviates from previous releases of the Qualitative Results in which the model was run both with and without frozen non-contiguous U.S. and insular support.

As explained below, the Bureau, by shoehorning Puerto Rico into the CACM, would effectively slash PRT's USF support by almost 90 percent—while increasing mainland support by 67 percent. This result is absurd given that the Commission has repeatedly found that insular territories like Puerto Rico have far lower broadband deployment and subscribership rates than any U.S. state and that residents of Puerto Rico comprise more than ten percent of the U.S. citizens without broadband today.[8] Further, such action by the Bureau would prevent the Commission from accomplishing its goal of universal broadband access and violate the Commission's express instructions to the Bureau in the *2011 USF Transformation Order*. Not only would such an approach be flawed as a matter of broadband policy, it also would suffer from serious legal flaws if adopted by the Bureau. *First*, the Bureau would exceed its delegated authority by ignoring the Commission's explicit instruction to make the "model and all underlying data, formulae, computations, and software associated with the model … available to all interested parties for review and comment."[9] *Second*, the Bureau's delegation of decision-making authority to CostQuest to build and operate the CAF II cost model would violate the D.C. Circuit's "subdelegation doctrine" and would render the entire cost model legally infirm because "black box" or hidden algorithms substantially determine the model's results. *Third*, the Bureau would violate the Administrative Procedure Act's ("APA") notice and comment requirements if it calculates insular support via CostQuest's proprietary CACM because it is riddled with hidden algorithms and erroneous assumptions that prevent PRT and other third parties from even attempting to evaluate the model's accuracy. For the forgoing reasons, the

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8 *Eighth Section 706 Report*, Apps. C, D.

9 *2011 USF Transformation Order*, ¶ 185.

Bureau should either accommodate the "unique circumstances" of insular areas in its model or maintain existing frozen high cost support for these areas.

II. PURSUANT TO THE COMMISSION'S INSTRUCTIONS IN THE *2011 USF TRANSFORMATION ORDER*, THE BUREAU SHOULD EITHER USE PRT'S COST MODEL TO CALCULATE SUPPORT FOR PUERTO RICO OR FREEZE PUERTO RICO'S EXISTING SUPPORT.

The record evidence shows that insular areas lag far behind the rest of the country in voice and broadband deployment, that insular areas are much more expensive to serve than non-insular areas, and that insular carriers serve the poorest populations in the country, which invariably results in low customer adoption rates.[10] The Commission recognizes this and instructed the Bureau in the *2011 USF Transformation Order* to "consider the unique circumstances" of non-contiguous U.S. and insular areas "when adopting a cost model."[11] The Commission further directed the Bureau to "consider whether the model ultimately adopted adequately accounts for the costs faced by carriers serving these areas."[12] The Commission's

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10 *See, e.g.*, *Eighth Section 706 Report*, App. C (presenting data that highlights just how underserved Puerto Rico is compared to the rest of the country); Letter from Thomas J. Navin, Outside Counsel, Puerto Rico Telephone Company, to Marlene H. Dortch, Secretary, FCC, WC Docket No. 10-90 (filed Sept. 12, 2012) (updating the record with the troubling data from the Eighth Broadband Progress Report); Comments of Puerto Rico Telephone Company, WC Docket No. 10-90 (filed Aug. 24, 2011) ("The Commission has recognized that most insular areas, like Puerto Rico, currently lag dramatically behind the rest of the nation in telephone and broadband subscribership and deployment."); Comments of Virgin Islands Telephone Corporation, GN Docket No. 11-16 (filed Mar. 2, 2011) (noting low broadband deployment in the U.S. Virgin Islands); Comments of Public Services Commission of the U.S. Virgin Islands, WC Docket No. 10-90, at 4-7 (filed Jul. 12, 2010) (discussing limitations on telecommunications infrastructure in the territory and challenges to deployment in the Virgin Islands); Comments of the Virgin Islands Telephone Corporation, CC Docket No. 96-45, at 15 (filed Nov. 3, 2000) (describing low penetration rates in the U.S. Virgin Islands).

11 *2011 USF Transformation Order*, ¶ 193. The Commission further instructed the Bureau to maintain existing frozen support levels for non-contiguous U.S. and insular areas if it cannot adopt a cost model that accounts for the unique costs of non-contiguous U.S. and insular areas. *Id.*

12 *Id.*

explicit purpose in establishing these requirements for insular areas was to ensure that adequate support was directed to those areas where extremely low rates of broadband penetration currently exist. The Commission stated that a model should not be adopted for use with insular areas if it "does not provide sufficient support to any of these areas."[13] The CACM—by slashing support to Puerto Rico by almost 90 percent—will not "preserve and advance the availability of voice service" or "ensure universal availability of modern networks capable of providing voice and broadband service to homes, businesses, and community anchor institutions."[14]

Indeed, as PRT previously detailed, the CACM does not "adequately account[]" for the costs of insular providers and thus does not pass the Commission's " insular test."[15] The CACM is a one-size-fits-all, forward-looking cost model that relies on hidden algorithms and inappropriate inputs designed for the U.S. mainland. In fact, under the model, support will plummet for Puerto Rico and other insular areas—the most underserved parts of America—but increase in the rest of the country despite the higher broadband deployment and penetration in these areas when compared to insular areas. In fact, under the CACM, unserved Puerto Ricans are almost completely ignored.[16] Indeed, based on the v.3.14 Illustrative Results, it is likely that out of the more than one million unserved customer locations the model will only provide support to 16,900 locations—a result that contravenes the Commission's goal of "ensur[ing] universal availability" of broadband-capable networks. Ultimately, the limited amount of support available for Puerto Rico under the current CACM—coupled with the parallel

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13 *Id.*

14 *Id.*, ¶ 17.

15 Comments of Puerto Rico Telephone Company, WC Docket No. 10-90, at 1 (July 9, 2012).

16 *See* CACM Report, Running Version 3.1.4.

elimination of existing high cost support—will actually slow down broadband penetration in Puerto Rico, which already lags well-behind the rest of the country. Accordingly, the Bureau should not use the current CACM to determine support for Puerto Rico.

Instead, the Bureau should either use PRT's "Broadband Cost Model: Puerto Rico" ("BCMPR") to allocate CAF II support for Puerto Rico or maintain frozen support. The BCMPR was created by an economic consulting firm that specializes in non-contiguous U.S. and insular costing. Further, the BCMPR—unlike the CACM—accurately accounts for the unique challenges and costs of deploying and offering broadband services in Puerto Rico while also placing a premium on cost efficiency. Accordingly, the BCMPR passes the Commission's "insular test" and should be used to calculate CAF II support for Puerto Rico—either as a standalone model or incorporated into a single model with the CACM.[17] If the Bureau does not adopt the BCMPR or a modified version of the model, it should at a minimum maintain existing high cost universal service support for the island coupled with adjustments to the CAF II public interest obligations required of PRT to reflect the receipt of support at levels deemed sufficient by the Commission only for the provision and operation of a voice network.

A. The CACM Fails the Commission's "Insular Test."

While the CACM may provide acceptable results for the contiguous 48 states, the model fails to account for the unique circumstances faced by carriers in insular areas. This is not surprising. As PRT previously explained, the model was not originally designed to handle

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[17] Although the BCMPR was filed six months ago, the Bureau has not asked PRT any questions about the model's algorithms, assumptions or input values. Nor has the Bureau asked for any supporting documentation or otherwise sought to understand the differences between the BCMPR—a model that was designed exclusively for an insular area—and the CACM—a model designed for the contiguous 48 states.

insular areas.[18] Rather, the model platform was built to model broadband deployment and operations for the mainland 48 states. Only as an afterthought were the non-contiguous and insular areas added. Moreover, none of the members of the coalition that designed the CACM (previously the CQBAT) are insular carriers. This is important since the CACM's inputs were determined based on the averaging of data supplied by the coalition members. Given that no insular carriers are members, no insular data were incorporated into the inputs. And while PRT, ACS, and VITELCO have each filed cost models with the Bureau, not until the last few weeks has the Bureau or CostQuest shown any interest in incorporating any inputs from these insular models into the CACM. Without inputs and assumptions from insular areas, as well as thorough testing that the results for insular carriers are reasonable, the CACM cannot be expected to adequately capture the costs specific to Puerto Rico and other insular areas.

The vast disparity in support for mainland and insular carriers under the CACM further demonstrates the model's inability to account for the unique costs of insular areas. As noted above, under CAF II, broadband funding for price cap carriers will increase from the current amount of $1.076B to $1.8B. This represents an across-the-board increase in support of 67 percent. The increased support is necessary because of the expanded requirements that carriers must meet under CAF II. But, based on PRT's analysis of the model's results under the $52/$174 benchmarks, the CACM would reduce support for PRT by almost 90 percent, from $36.8M to $3.8M annually.[19] Other insular areas would suffer a similar fate.[20] This reduction in

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18 *See* FCC Workshop on CAF Modeling (Sept. 14-15, 2012).

19 *See* FCC Illustrative Results, CACM v3.1.4, Scenario 2.1. PRT continues to believe that the National Broadband Map does not accurately depict the presence of unsubsidized cable competitors in Puerto Rico. Accordingly, for purposes of calculating PRT's support under the CACM and the BCMPR—and comparing the support derived under each model—PRT has not

support for insular areas is counterintuitive given: (1) the overall increase in support available to price cap carriers; (2) the increased obligations under CAF II; (3) the Commission's repeated acknowledgements that insular areas are much more expensive to serve than non-insular areas and that build-out in insular areas lags far behind the mainland U.S.; and (4) that Puerto Rico has more residents without broadband than any other U.S. state or territory. In order to meet the Commission's goal of universal availability of broadband capable networks, support for areas like Puerto Rico should increase under CAF II, just like it does for mainland price cap areas.

Notably, the CACM's laser-like focus on meeting the needs of mainland states to the detriment of insular areas manifests itself repeatedly in the CACM Cost Methodology. Listed below are several instances in which the CACM Cost Methodology fails to consider the unique costs of Puerto Rico and other insular areas—costs which if properly accounted for would likely result in much larger distributions to insular areas:

Internet Peering Points. The CACM assumes that the nearest Internet peering location is on a regional tandem located in the same LATA and connected by fiber.[21] While this may be the case for price cap carriers in the contiguous 48 states, the assumption does not hold for insular areas like Puerto Rico, as the Bureau itself seems to recognize.[22] Instead, Puerto Rico, like

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entered a figure for the "unsubsidized competitor" input. If such a figure is included, however, Puerto Rico's support would drop even further.

20 The CACM model would result in a 98 percent decrease in annual support for Virgin Island's VITELCO, from $16.5M to $.26M.

21 *Connect America Cost Model (CACM): Model Methodology*, CACM version 3.1.3, Document version 3.1.4, at p. 51-52 (revised 6/21/2013) ("CACM Model Methodology").

22 *See Wireline Competition Bureau Seeks Comment on Connect America Phase II Support for Price Cap Areas Outside of the Contiguous United States*, Public Notice, WC Docket No. 10-90, DA 13-162, at 8 (Wireline Bur. Feb. 8, 2013).

Alaska and the Virgin Islands, must connect to the Internet via thousands of miles of undersea cable.[23] As PRT has previously explained, the current CACM does not account for such costs.[24]

Residential and Business Demand Data. CostQuest admits that "[s]ervice location data are … key drivers of the network build and instrumental to [the] reliability of the results."[25] Unfortunately, the projected service location data that the CACM uses for Puerto Rico are far inferior to the GeoResults data used for the mainland. While CostQuest trumpets the accuracy of the GeoResults data for the 50 states and D.C.—highlighting that approximately 96 percent of residences and 94 percent of business are considered to be "well geocoded"[26]—no such claims can be made for Puerto Rico, for which no such data exist.[27] Instead, CostQuest relies on US Census, SF1 data, which CostQuest then randomly assigns to road locations with Puerto Rico's

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23 The three non-contiguous U.S. and insular cost models, however, calculate the cost of the submarine cable needed to transport Internet traffic to the nearest peering location on the mainland. PRT's model calculates the cost of transporting Internet traffic across its MPLS network to its Internet core and then to an undersea cable that terminates in Miami or Jacksonville, Florida. These undersea cable costs are shown in PRT's filed model and are based on the cost to PRT of obtaining Indefeasible Rights of Use on existing cables from the Island to Florida. In contrast, the CACM model assumes that the nearest peering point is located at a regional tandem in the same LATA. In PRT's case, this would mean that the CACM would only include the transport cost from the origination point somewhere in Puerto Rico to either of PRT's two tandems in the San Juan area. The VITELCO model develops the submarine transport cost in the same manner, while the ACS model calculates the cost based on its costs of building its own cable from Alaska to Oregon in 2009.

24 *See* Comments of Puerto Rico Telephone Company, Inc., WC Docket No. 10-90, at 4 (March 11, 2013).

25 *See* CACM Model Methodology at § 5.2.3.2 (emphasis added).

26 *See id.*

27 For the 50 states and D.C., the CACM relies on address level data from GeoResults that has been geocoded and associated with the nearest road point to allow a network to be created through spatial programming. For Puerto Rico, however, no GeoResults data exist. *See id.* at § 3.2.

Census Blocks.[28] Without the GeoResults data for Puerto Rico—which CostQuest highlights as offering the most accurate placement of customer locations on roads within a census block—the CACM's results for Puerto Rico are necessarily less accurate than CACM's results for the rest of the country.[29]

Importantly, PRT provided the Bureau and CostQuest with a way to address this disparate treatment. Specifically, the BCMPR provides actual route feet over which PRT will need to deploy broadband to all Puerto Ricans—served and unserved. These cable quantity data could have been integrated into the CACM to provide more accurate results for Puerto Rico. But neither the Bureau nor CostQuest took advantage of this granular information, despite being apprised of its availability and relevance during an ex parte meeting with PRT on January 24, 2013.[30]

Voice Costs. CostQuest assumes that the IP Multimedia Sub-System (IMS)/Softswitching platform—which provides routing information for voice packets—will be deployed as a "national architecture that supports multiple states with *one or more paired core sites* that contain modules sized to meet demand required and multiple access sites that interconnect with other carriers that feed into the core sites."[31] This assumption does not work when forecasting build-out costs for Puerto Rico. Indeed, in Puerto Rico, core sites will reside exclusively within the island and will be constructed and operated exclusively by PRT. The

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28 *See id.*

29 *See id.*

30 *See* Letter from Thomas J. Navin, Counsel for PRT, to Marlene Dortch, Secretary, FCC, WC Docket No. 10-90 (Jan. 28, 2013) (memorializing PRT's meetings with the Bureau and Commissioner advisors).

31 CACM Model Methodology at § 5.2.3.4 (emphasis added).

CACM erroneously assumes that PRT will be able to leverage investments in switching facilities made by other carriers. In fact, PRT—unlike mainland carriers—will be unable to leverage switching investments and large volume purchasing power in equipment and labor across service areas covering multiple states that dwarf Puerto Rico's 3,500 square mile area.

Operational Cost Development Process. The CACM estimates the operating costs of medium-sized carriers such as PRT by reducing the operating expense factors for Cable and Wire Facilities ("CWF") of the largest carriers by 26.96 percent.[32] In fact, the table below shows that—all else being equal—the medium-sized company CWF maintenance factors found in the model yield the lowest support levels for PRT.

FCC Illustrative CACM v3.1.4 Scenario 2.1[33]

ID	Description	Funding	Locations
xx	CACM v3.1.4 Baseline OCN Co Size Medium	$ 3,838,514	16,939
57A	CACM v3.1.4 w/ OCN Co Size Small	$ 4,888,770	21,713
58B	CACM v3.1.4 w/ OCN Co Size Large	$ 3,947,765	17,586

As described in the OPEX Overview provided as part of the CACM documentation, these factors were based on Part 32 Account data averaged across companies in the same size class and adjusted for spreads between current and book asset values. As the results above indicate, the CACM erroneously assumes that insular carriers are operationally more efficient with regard to cable and wire facilities than larger carriers, despite the economies of scale from which larger carriers benefit during broadband deployment. That the CACM increases the CWF maintenance factors for small, extra small, and double-extra small companies by 29.59 percent, 47.82 percent,

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32 *See* Input File: Opex V7, Tab: Telco Opex, cells P9 – P16.

33 $52 Lower Benchmark, $122.483 Alt Tech Cutoff, $174.483 Upper Benchmark, Results for PRT at 9 percent COM.

and 64.33 percent respectively—but decreases the factor for medium carriers—only further highlights the CACM's erroneous constructions. In effect, the model captures the economies of scale impact for every classification but the medium classification—into which PRT falls.

Documentation on the USAC website explains that the final CWF factor values were adjusted to ensure that the modeled forward-looking OPEX did not exceed booked OPEX.[34] But this adjustment cannot explain why when setting the company size variable for PRT to "L" (for large company) the estimated support exceeds the estimated support when setting the size variable to "M" (for a medium size company).[35]

Build and Take Rate Assumptions. In the latest Illustrative runs of the CACM, unit costs are determined by dividing total cost by all available locations regardless of whether the locations are expected to take service. In effect, this assumes a 100 percent take rate and would result in the lowest possible cost per customer location.[36] The Illustrative runs also incorporate a nationwide take rate of 80 percent by setting the lower benchmark equal to 80 percent of the assumed average revenue per unit of $65 per subscriber. However, this fails to appreciate that the take rates in insular areas like Puerto Rico trail well-behind mainland take rates. In fact, based on PRT's marketing research, actual take rates in Puerto Rico range from 25 to 35 percent in areas where broadband service is available. Even assuming that the increased availability of broadband over the five-year life of the CAF II program will increase take rates across the island, it is extremely unlikely that Puerto Rico will achieve an 80 percent take rate over this period. As

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34 *See* Opex Overview, pg. 13, *available at* https://cacm.usac.org/resources.aspx.

35 *See* Input File: Opex V7, Tab: Telco Opex, cells P9 – S16.

36 CACM Cost Methodology at § 5.2.1 at Table 2.

PRT has previously explained to the Commission, the low take rates likely result from the extremely low personal income levels in the territory relative to the mainland U.S.[37]

B. The BCMPR Passes the "Insular Test."

Unlike the CACM, the BCMPR uses a Puerto Rico-specific set of granular inputs to determine the cost of providing broadband in Puerto Rico consistent with the Commission's CAF II requirements. Specifically, the model:

- Builds off of data and information contained in the Puerto Rico Forward-Looking Model, versions of which have been used to determine UNE rates by Puerto Rico's Telecommunications Regulatory Board for the past sixteen years;
- Uses a modified "greenfield" approach based on a 2009 Right-Of-Way ("ROW") study commissioned by PRT in response to new ROW tax legislation to develop the forward-looking cable routes and cable quantities required to develop forward-looking cost;
- Includes the cost of the off-island transport and Internet peering provided via undersea cable from Puerto Rico to the Internet peering location in Florida based on the actual annual costs incurred by PRT to purchase capacity on undersea cable facilities today;
- Uses Puerto Rico-specific costs for the acquisition, engineering, and installation prices for broadband transmission equipment (*e.g.*, routers, DSLAMS, etc.) and for material, engineering, and installation costs of fiber and copper outside plant;
- Uses inputs based on PRT's internal capital budgeting process that creates incentives to develop input values that reflect a cost-efficient approach to deploying and operating network facilities;
- Allows users to review, analyze, and change all assumptions, algorithms and formulas contained in the model, unlike the CACM. This feature will allow reviewers to evaluate in real-time the impact of any changes made to the model[38]; and
- Unlike the CACM, allows users to identify and analyze the quantity of each type of material and equipment used in the simulated broadband-capable network.

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37 *See* Letter from Thomas J. Navin, Counsel for PRT, to Marlene Dortch, Secretary, FCC, WC Docket No. 10-90, at Attachment A "Broadband Cost Model: Insular Area Broadband Network Economic Cost Simulation for Puerto Rico," at n. 7 (Jan. 18, 2013).

38 The model's structure is flexible in order to utilize the unique customer location and input data available for a specific non-contiguous U.S. area. As such, the framework is designed to be applied to any non-contiguous U.S. carrier.

By using Puerto Rico-specific input prices, network topology requirements, territory-specific road and outside plant structure data, and labor costs, the BCMPR clearly accounts for the real costs facing carriers that service this insular area. When these unique costs are accounted for in the BCMPR—and the BCMPR is adjusted to incorporate the Bureau's current parameters—support for Puerto Rico increases from the current amount of $36.8M to approximately $80M.[39] This is in stark contrast to the CACM's determination that support for PRT should decrease by $33 million. This increase in funding from present levels makes achieving the broadband requirements of CAF II a possibility. Further, this increase in funding is appropriate in light of the 67 percent overall increase in funding for all price cap carriers under CAF II.

C. The June 10 Letter Erroneously Asserts that the Insular Carrier "Submissions Received to Date Are Insufficient."

PRT and other insular carriers have been active participants in the CAF II proceeding. And they have invested significant time and money in developing the BCMPR and other insular cost models to help the Bureau develop mechanisms that properly account for the unique costs of insular areas—as required by the Communications Act and the Commission. Given these facts, the suggestion in the June 10 letter that PRT and other insular carriers have failed to provide sufficient information to the Bureau to determine the necessary level of support for insular areas misses the mark.[40]

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[39] This support amount is calculated based on the following assumptions: (1) a total number of customer locations of 1.75M; (2) a take rate for broadband services of 80 percent; (3) upper and lower benchmarks of $174 and $52, respectively; (4) a cost of capital of 9 percent; and (5) transport via undersea cable from Puerto Rico to peering location in Florida.

[40] *See* Wireline Bureau June 10 Letter at 1 ("Bureau representatives indicated that the outside parties' submissions received to date are insufficient in helping the Bureau understand

As shown above, the BCMPR provides the Bureau with more than enough verifiable data to craft an equitable, insular-specific cost model. The BCMPR and the other cost models also include full sets of inputs regarding the costs to deploy and operate networks in these areas, and these inputs could be incorporated into any larger, all-encompassing model. Indeed, each model contains much of the demand, demographic, material, equipment, and labor cost inputs required to simulate the build-out of a broadband network in insular areas.

Accordingly, PRT is puzzled by the recent assertion in the June 10 letter that insular carrier "submissions received to date are insufficient."[41] PRT's model was filed six months ago.[42] During this time, the Bureau did not ask PRT to explain its model's inputs, nor did the Bureau raise any specific concerns regarding PRT's model. This lack of investigation of PRT's model significantly undermines the Bureau's claim of the insufficiency of data on insular areas.

D. If the Bureau Cannot Accommodate Insular Areas in its Model, it Must Maintain Frozen Support.

In its *2011 USF Transformation Order*, the Commission recognized the unique challenges of serving non-contiguous U.S. and insular areas and specifically directed the Bureau to (1) adopt a cost model that adequately accounts for the unique costs of serving non-contiguous U.S. and insular areas; or (2) maintain existing frozen support levels for those non-contiguous U.S. and insular areas left out of the cost model.[43] This approach would still support broadband deployment because the Commission has required that "all carriers receiving frozen high-cost

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how to better account for the operating conditions and challenges these carriers face in non-contiguous areas.").

41 Nor has the Bureau provided any analysis that supports its implication that current support levels are inflated for insular carriers. *See* Public Notice DA 13-162.

42 VITELCO also recently filed a model.

43 *2011 USF Transformation Order*, ¶ 193.

support use at least one-third of that support to build and operate broadband-capable networks ...."[44] Further, for "2014, at least two-thirds of the frozen high-cost support must be used in such fashion, and for 2015 and subsequent years, all of the frozen high-cost support must be spent in such fashion."[45]

III. ANY ACTION RELYING ON THE CACM AND ITS UNDERLYING DATA WOULD EXCEED THE BUREAU'S DELEGATED AUTHORITY IF THE PUBLIC DOES NOT HAVE OPEN ACCESS TO THE CACM AND ITS UNDERLYING DATA.

Absent open access to the CACM and its underlying data, any Bureau action applying the CACM to insular areas will exceed the scope of the Bureau's delegated authority. In the *USF/ICC Transformation Order*, the Commission emphasized that the model and the input values used to determine support amounts in particular areas must be available for review by the public. Specifically, the "model and all underlying data, formulae, computations, and software associated with the model must be available to all interested parties for review and comment."[46] And "[a]ll underlying data should be verifiable, engineering assumptions reasonable, and outputs plausible."[47] Moreover, the public must have access to the underlying source code as well as the input data, in order to test the model by changing input values, running sensitivity tests, and comparing the results of various runs of the model.[48] Contrary to the Commission's instructions, the Bureau thus far has foreclosed PRT and the rest of the public from accessing basic information about the workings of CostQuest's proprietary model components—the CQLL and

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44 *Id.*

45 *Id.*

46 *Id.*, ¶ 185.

47 *Id.*

48 *Request for Connect America Fund Cost Models*, Public Notice, DA 11-2026, ¶ 4 (Wireline Comp. Bur. rel. Dec. 15, 2011).

CQMM modules. In rejecting the Commission's clear instructions, the Bureau has acted contrary to its delegated authority. And the Bureau's work product—which is really CostQuest's work product—and any future models derived from this work product will not be legally sustainable.[49]

IV. ANY USE OF THE CACM FOR INSULAR AREAS WOULD BE AN UNLAWFUL SUBDELEGATION OF DECISION-MAKING POWER TO COSTQUEST.

Under D.C. Circuit precedent, federal agency officials "may not subdelegate [their decision-making authority] to outside entities—private or sovereign—absent affirmative evidence of authority to do so."[50] This prohibition stems from the court's determination that "[a] general delegation of decision-making authority to a federal administrative agency does *not*, in the ordinary course of things, include the power to subdelegate that authority beyond federal

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[49] *See, e.g.*, *In the Matters of Responsible Accounting Officer Letter 20, Unif. Accounting for Postretirement Benefits Other Than Pensions in Part 32 Amendments to Part 65, Interstate Rate of Return Prescription Procedures & Methodologies, Subpart g, Rate Base*, Memorandum Opinion and Order, 11 FCC Rcd 2957, ¶ 25 (1996) (granting application for review of the Common Carrier Bureau's ratemaking instructions on the grounds that the Bureau exceeded its authority by directing exclusions from and additions to a rate base "for which the Part 65 rules do not specifically provide"); *In the Matter of Applications of Little Dixie Radio, Inc., Assignor & Kesc Enterprises, LLC, Assignee Little Dixie Radio, Inc., Assignor & Se. Oklahoma Radio, LLC, Assignee Bottom Line Broad., Inc., Assignor & Se. Oklahoma Radio, LLC, Assignee*, Memorandum Opinion and Order, 25 FCC Rcd 4375, ¶ 5 (2010) (holding that the Media Bureau exceeded its delegated authority by departing from the Commission's *Jefferson Radio* policy and by granting a broadcaster's assignment application while the character qualification of the assignor remained in issue); *In Re Applications of Tully-Warwick Corp. Concord, New Hampshire Req: 1140 Khz, 5 Kw, Da-D Concord Broad. Associates Concord, New Hampshire Req: 1140 Khz, 10 Kw, Da-D for Constr. Permit*, Memorandum Opinion and Order, 95 FCC 2d 1427, ¶ 5 (1983) (holding that the Media Bureau exceeded its delegated authority by designating for filing broadcast applications where such designation was not specifically permitted by the Commission's rules or Commission precedent).

[50] *U.S. Telecom Ass'n v. F.C.C.*, 359 F.3d 554, 566 (D.C. Cir. 2004) (citing *Shook v. District of Columbia Fin. Responsibility & Mgmt. Assistance Auth.*, 132 F.3d 775, 783–84 (D.C. Cir. 1998)).

subordinates."[51] Moreover, when an agency "delegates power to outside parties," lines of accountability "may blur, undermining an important democratic check on government decision-making."[52] Here, use of the CACM would plainly violate the "subdelegation doctrine" if the effect is to delegate decision-making authority to CostQuest to build and operate the CACM for insular areas even though neither the Communications Act nor any other statute empowers the Bureau (or Commission) to subdelegate such authority to a private entity.[53] Accordingly, the Bureau may not use the CACM to allocate CAF II support to insular areas.

The CACM is a lightly-modified version of the ABC Cost Model, which CostQuest originally developed as a paid consultant for the nation's largest price cap carriers and which initially excluded PRT. Although the Bureau—through USAC—has since contracted with CostQuest to have some nominal stake in the model's design, the models are markedly similar. The Bureau itself admits to delegating its responsibility to create the CACM to CostQuest. Indeed, the Bureau recently explained that the Commission gave it "the task of selecting a specific engineering cost model and associated inputs that meet the criteria specified in the USF/ICC Transformation Order."[54] But "[i]n order to provide the Commission with a potential

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51 *Id.* (emphasis in original).

52 *Id.* at 565-566 (citing *NARUC*, 737 F.2d at 1143, n. 41). In addition, the delegation of authority to outside parties increases the "risk that these parties will not share the agency's national vision and perspective and thus may pursue goals inconsistent with those of the agency and the underlying statutory scheme." *Id.* at 566 (internal quotations omitted). "In short, subdelegation to outside entities aggravates the risk of policy drift inherent in any principal-agent relationship." *Id.*

53 And this statutory "'silence' simply leaves that lack of authority untouched." *Id.* Indeed, the "failure of Congress to use 'Thou Shalt Not' language" does not empower the Commission with the discretion to subdelegate this matter. *Id.*

54 *Connect America Fund*, Third Supplemental Protective Order, 27 FCC Rcd 15277, ¶ 2 (Wireline Bur. Dec. 11, 2012).

model," the Bureau—through USAC—"*contracted with [CostQuest] to develop the [CACM]*...."[55]

Further, the "CACM" is clearly "a proprietary software application *owned* by CostQuest."[56] As creator and owner of the model, CostQuest—not the Bureau—has crafted the hidden algorithms, input sheets, and toggle formulae that power the CACM. This includes the algorithms contained in the proprietary CQLL and CQMM modules—the modules that dictate how CAF II-funded broadband networks will be designed and built. In doing so, CostQuest has necessarily made policy decisions that affect how CAF II support will be allocated which the Bureau will not be able to approve or endorse because they are simply a "black box" to anyone using the model.

Indeed, it bears emphasis that the power that the Bureau has contracted out—or "subdelegated" to CostQuest—is not merely ministerial. The power to build the model for broadband support is the power to ultimately determine the amount and extent of such support. By allowing CostQuest to "make crucial decisions" about the inputs and assumptions that the model will employ, the Bureau would be abdicating core decision-making functions to this private entity, "with FCC oversight neither timely nor assured."[57] In short, what the Bureau has

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55 *Id.* (emphasis added).

56 *Id.*, ¶ 4 (emphasis added). The portion of USAC's website that hosts the CACM also emphasizes that the CACM "system is the property of CostQuest" and that "CostQuest reserves all rights in CACM." *See* "Connect America Cost Model: Developed by CostQuest Associates," USAC, https://cacm.usac.org/login.aspx?ReturnUrl=%2f. Likewise, the CACM Model Methodology has been copyrighted by CostQuest. *See* CACM Model Methodology at 2.

57 *U.S. Telecom Ass'n*, 359 F.3d at 567.

done is simply an "attempted punt" of basic federal governmental responsibility under the universal service statute.[58]

Although the Bureau has solicited input on ways to tweak CostQuest's model, the public's input—particularly as it relates to insular areas—has fallen on deaf ears.[59] The Bureau repeatedly has refused to address questions and concerns from PRT regarding the CACM. Instead, it has punted PRT's questions regarding the model's construction, operations, and outputs to CostQuest, telling insular carriers to seek answers "through CostQuest's Help Desk ticketing process."[60]

As the CAF II distribution proceeding winds down, there is no way now to cure the violation of the subdelegation doctrine. Although agencies may lawfully consult with private parties for advice and fact-gathering,[61] CostQuest's role in this proceeding far exceeded either of these narrow exceptions. As explained above, CostQuest—in designing the model and its proprietary algorithms—has made crucial policy decisions that will determine how $1.8B in CAF II support is distributed. At this late stage in the proceeding, the Bureau may not "merely 'rubber-stamp' decisions" by CostQuest "under the guise of seeking [CostQuest's] 'advice', nor will vague or inadequate assertions of final reviewing authority save" the Bureau's "unlawful subdelegation."[62] Nor does the abdication to CostQuest of the entire modeling process "remotely

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58 *Id.*

59 *See supra* Section II.C.

60 Wireline Bureau June 10 Letter at 2.

61 *U.S. Telecom Ass'n*, 359 F.3d at 566-568.

62 *Id.* at 568 (internal citations omitted).

resemble" the type of legally permissible "nondiscretionary information gathering" that the D.C. Circuit might consider permissible.[63]

V. THE BUREAU'S RELIANCE ON A PROPRIETARY MODEL THAT IS NOT OPEN FOR PUBLIC REVIEW TO DISTRIBUTE SUPPORT TO INSULAR AREAS VIOLATES THE APA.

The use of a proprietary CACM to allocate insular support would also violate the APA's notice and comment requirements. In construing the APA's notice and comment requirements, the D.C. Circuit explained long ago that "[i]n order to allow for useful criticism, it is especially important for the agency to identify and make available technical studies and data that it has employed in reaching the decisions to propose particular rules."[64] Indeed, public notice and comment regarding a "relied-upon technical analysis" are "[t]he safety valves in the use of ... sophisticated methodology."[65] When an agency fails to make such information publicly available, any rules that it adopts and regulatory actions it takes based on the information violate the APA.

Here, the CACM, like the CQBAT model before it, suffers from a lack of transparency and inflexibility. The model cannot be meaningfully understood by the public without improved access to the mechanisms and greater disclosure of the assumptions that underlie it. Insular carriers simply cannot reproduce or validate the results of the current CACM because the public does not have access to all the meetings, discussions, analyses, and workpapers that led to the development of the model's inputs and hidden algorithms. Nor do carriers have access to the

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63 *Id.* at 566.

64 *Conn. Light & Power Co. v. Nuclear Regulatory Comm'n*, 673 F.2d 525, 530 (D.C. Cir. 1982); *see also Am. Radio Relay League, Inc. v. F.C.C.*, 524 F.3d 227, 236 (D.C. Cir. 2008) (remanding a FCC rule because of the agency's failure to provide the public with access to unredacted technical studies and data that it employed in reaching its decisions).

65 *Am. Radio Relay League, Inc.*, 524 F.3d at 236.

CQLL and CQMM—proprietary modules owned by CostQuest—even though these modules dictate how the broadband networks will be designed and built and generate the quantity of materials and equipment that will be basis for the cost estimation. Accordingly, carriers impacted by the model cannot run the model in real time to assess the value of changes.

The CACM Model Methodology itself is replete with admissions that CostQuest relied on hidden algorithms and inputs in order to construct the CACM. Examples include:

- *CQLL and CQMM*: the proprietary design and build modules owned by CostQuest that dictate the quantity of materials and equipment used in the model.

- *OpEx Assumptions*
  - *Opex Factor Adjustment*. CostQuest fails to explain how it "adjusted" the "historic financial data comprised of mixed technological generations" to "predict the operating expense of deployed new technology…."[66]

  - *Network Operations Expenses*. CostQuest explains that "[t]o estimate the CACM Network Operations Expenses, the relationship between capital investment and ongoing cost to operate and maintain the plant was determined."[67] And this "determination relied primarily on three years of NECA data (2008-2010), supplemented with *additional data sourced from … third party sources*[,]" including "material provided by the ABC Coalition companies."[68] But CostQuest fails to explain if the data provided by the ABC Coalition companies is available to third-parties for review.

  - *Opex to Plant Investment Factor*. CostQuest fails to explain how the "NECA-based Opex to Plant Investment factor" was "adjusted from a historical cost basis to a contemporary topology specific network build on a forward-looking cost ("FLC") basis, resulting in the baseline CACM Opex Sub-Module factors."[69]

  - *Customer Operations Marketing & Service Operating Expenses*. To determine the CACM customer selling and marketing OpEx Sub-Module

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66 CACM Methodology at § 5.3.1(e).

67 *Id.* at § 5.3.3.1.

68 *Id.* at n. 19 (emphasis added).

69 *Id.*

> factor, CostQuest relied in part on ABC Coalition company data that are not available to PRT or other third parties.[70]

These examples reflect the fundamental lack of transparency that has enveloped the entire cost modeling process. And so long as these inputs and algorithms remain unknown, the CACM will remain legally untenable.[71]

Finally, it is worth noting that other carriers have raised similar concerns and requested information from the Bureau and CostQuest to allay these concerns. Like PRT, however, these carriers have not received substantive responses from the Bureau or CostQuest. For example, on May 11, 2012, ACS submitted over 150 granular questions and requests for information to the Bureau and CostQuest regarding the CACM's construction.[72] ACS—and PRT—believe that these questions and requests merited a response in order to ensure that the input values, computations, and formulae embodied in the CACM can be fairly examined and understood by the public and the Commission. To PRT's knowledge, however, neither the Bureau nor CostQuest ever responded.

VI. CONCLUSION

For the foregoing reasons, PRT urges the Bureau to base its decisions on the Commission's clear instructions and ensure that insular areas are treated fairly during CAF Phase

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70 *See id.* at § 5.3.3.3.

71 Perhaps most troubling, the Bureau never responded to the numerous comments that asked why the CACM would distribute support that is 90 percent less than what PRT currently receives, 97 percent less than what VITELCO currently receives, and 67 percent below what ACS currently receives, even though support spiked by 67 percent nationwide for price cap carriers as a whole.

72 *See* Letter from Karen Brinkmann, Counsel to ACS, to Marlene Dortch, Secretary, FCC, WC Docket No. 10-90 (filed May 11, 2012).

II by either accommodating them through a transparent model or by maintaining their frozen support.

Respectfully submitted:

Francisco J. Silva
Walter Arroyo
PUERTO RICO TELEPHONE COMPANY, INC.

By: *Thomas J. Navin*

Nancy J. Victory
Thomas J. Navin
WILEY REIN LLP
1776 K Street, NW
Washington, DC 20006
(202) 719-7000

Counsel for Puerto Rico Telephone Company, Inc.

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